

"We contend that for a nation to try to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handles."  
Sir Winston Churchill

## ECONOMIC OUTLOOK

In his first congressional testimony since being elected chairman of the US Federal Reserve (the Fed), Jerome Powell reiterated that the US economy remained strong and the Fed would continue raising interest rates gradually. He did indicate that economic momentum had accelerated since December, following the recently announced \$1.5 trillion tax cuts. At this stage, the market expects the Fed to raise interest rates three times in 2018. With the US economy now at full employment, wages have started rising, which could cause consumer inflation to rise above the Fed's target of 2%. The risk is therefore that the Fed is forced to hike interest rates at least four times this year, although given the indebtedness of the US government, they would prefer interest rates to remain low.

The European Central Bank (ECB) is facing a similar dilemma, as inflation has started to accelerate. Although economic activity continues to grow, the rate of growth is modest when compared to the US and the political backdrop remains uncertain as Italians go to the polls in March and Angela Merkel struggles to form a coalition government in Germany. The ECB plans to continue buying €30 billion worth of bonds a month until at least September, to stimulate economic growth in the region. The euro has strengthened since the end of the year, which is dampening appetite for Europe's exports and undermining Germany's growth prospects.

Index	February %	12m %	YTD %
Dow Jones	-4.0	23.1	1.7
S&P 500	-3.7	17.1	1.8
FTSE 100	-4.0	-0.4	-5.9
EURO STOXX 50	-4.6	6.2	-1.7
Nikkei 225	-4.5	15.4	-3.1
Hang Seng	-6.2	29.9	3.1
Australia	-0.5	6.9	-0.8

Source: I-Net Bridge

In South Africa, President Jacob Zuma resigned and was replaced by ANC President, Cyril Ramaphosa. Zuma's resignation resulted in significant rand strength in the first half of February (chart 1). Ramaphosa has moved swiftly to remove many ministers implicated in state capture, recalling both Nhlanhla Nene as minister of finance and Pravin Gordhan as minister of public enterprises. Gwede Mantashe has replaced Mosebenzi Zwane as minister of minerals and energy. The cabinet reshuffle also included the appointment of David Mabuza as Deputy President of the country following his election as Deputy President of the ANC in December last year.

The budget, delivered in parliament by Finance Minister, Malusi Gigaba, was well received by the market. The budget painted a slightly more upbeat picture as a combination of fiscal measures and higher GDP growth should deliver progressively lower budget deficits over the next three years, despite the introduction of free-fee education announced by President Jacob Zuma at the end of last year. The bulk of the adjustments to the budgeting process were on the revenue side, which included the first VAT increase in 25 years. The improved budget should ensure that Moody's delays its decision to cut South Africa's credit rating.

## MARKET OUTLOOK

Global equity markets fell sharply in February on concerns the Fed would need to raise interest rates more aggressively as wage inflation accelerates in the US. The S&P 500 declined by 3.7% in February, but was down as much as 8.6% during the month before recovering in the final two weeks. Over the past 12 months, the S&P 500 index is up 17.1% (chart 2). Global equity markets have been buoyed by the prospects of interest rates remaining lower for longer but recent comments from central bankers suggest monetary policy may become less accommodative throughout 2018 and 2019. Investors are now having to weigh up the impact of higher interest rates against the prospect of higher earnings growth, following tax cuts in the US.

Bond yields in the US continue to move higher (chart 3), although yields in Europe remained largely unchanged. US investors are jittery following comments by Jerome Powell that economic growth was accelerating and that the Fed was ready to act to maintain price stability, defined as consumer inflation at or around 2%. The US is also forecast to issue a record number of bonds in 2018 which may exceed current demand. The global equity market sell-off, combined with the sharp increase in US bond yields drove global listed property prices sharply lower. The GPR 250 REIT index declined by 6.5% in US dollars in February (chart4).

Index	February %	12m %	YTD %
All Share	-2.0	17.4	-1.9
Resources	-4.8	16.1	-1.8
Financials	2.6	20.5	-0.5
Industrials	-3.0	16.6	-2.6
Property	-9.9	-6.1	-18.8
Bond	3.9	14.3	5.9
Cash	0.5	7.5	1.1

Source: I-Net Bridge

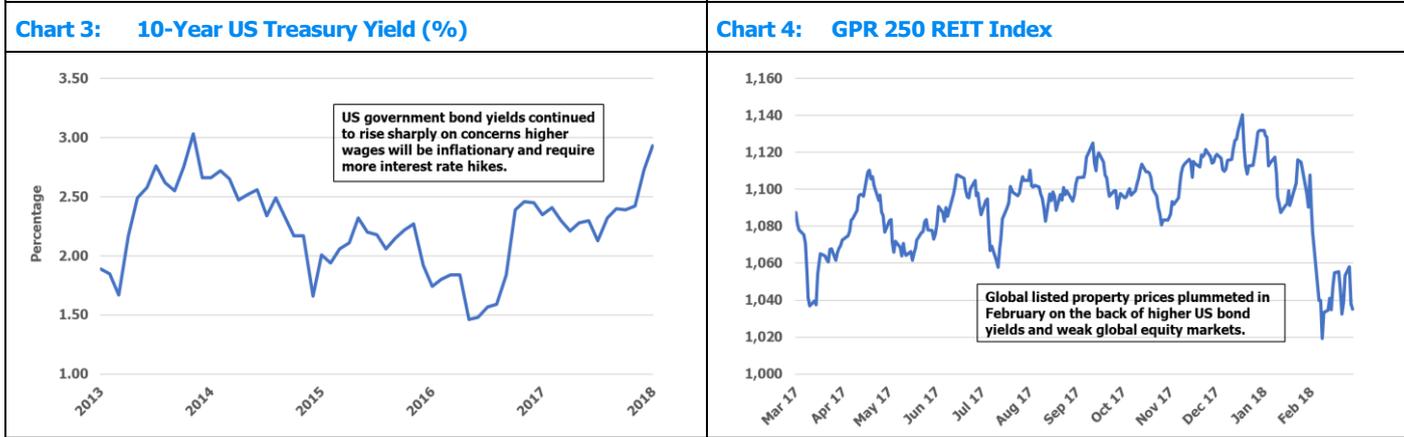
Despite falling 2% in February (chart 5), the South African equity market was one of the best performing equity markets during the month. While the rand's strength and lower commodity prices pushed the resources sector lower, those companies with a strong domestic focus continued to push higher. Since the ANC's elective conference, the South African equity market has been dominated by the so-called "SA Inc" shares, while the resources sector and large rand-hedge industrial companies have lagged. The banks and retailers have been particularly strong as investors continue to bet on a revival in South Africa's economic fortunes.

South African government bond yields maintained their positive momentum in February. The yield on government's benchmark R186 bond has now fallen to 8.12% (chart 6). In the South African listed property sector, the Resilient group of companies continued to suffer material price declines in February following the release of two research documents that alleged shares prices of the Resilient group of companies had been manipulated. The SA listed property sector is down 18.8% this year, with the losses attributable to the Resilient group of companies as well as the non-South African property companies listed on the JSE.

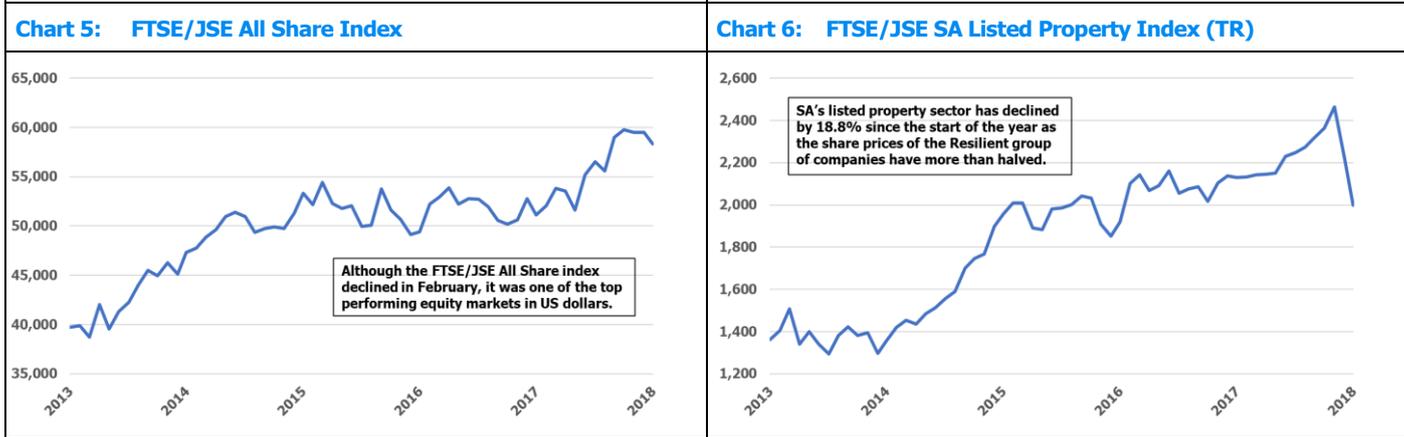
## CHARTS



Source: I-Net Bridge



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